United States Court of Appeals

for the Second Circuit

REPLY BRIEF

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P/S

74-20832

ORIGINAL

United States Court of Appeals

FOR THE SECOND CIRCUIT

FOTOCHROME, INC.,

Debtor-Appellant,

—against—

COPAL COMPANY, LIMITED,

Claimant-Appellee.

REPLY BRIEF OF DEBTOR-APPELLANT FOTOCHROME, INC.

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UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

FOTOCHROME, INC.,

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-against-

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Docket Number 74-2083

Reply Brief of Debtor-Appellant Fotochrome, Inc.

Statement

This brief is submitted on behalf of Debtor-Appellant Fotochrome, Inc. in reply to the answering brief of Claimant-Appellee Copal Company, Limited.

POINT I

Fotochrome Did Not Withdraw from the Arbitration

It has already been noted that Fotochrome as debtor in possession had the power and title of a trustee in bankruptcy, but that it was subject to the control of the bankruptcy court. Section 342 of the Bankruptcy Act (11 U.S.C. §742). The referee's order, although lacking the jurisdictional prerequisites to effectively stay Copal and the Japan CAA from proceeding with the arbitration, did prohibit Fotochrome from appearing before the arbitration panel. Although notified of the referee's action, Copal successfully urged the Japan CAA to conclude the arbitration without hearing Fotochrome's defense or evidence in support of its counterclaim. Copal's insistence upon proceeding to a conclusion without granting Fotochrome the opportunity to present its case constituted, by American standards, a denial of due process.

An award obtained in an arbitration conducted without regard to due process of law is, obviously, not one conducted in accordance with the Bankruptcy Act, and as such, does not constitute a provable debt under Section 63(a)(5) of the Bankruptcy Act [11 U.S.C. §103(a)(5)]. Proceedings conducted without regard to due process are excepted from

the arbitration enforcement provisions of the Treaty with Japan on Friendship, Commerce and Navigation (Art. IV, para. 2, 4 U.S.T. 2063) and the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (Art. III and V, 21 U.S.T. 2517 at 2519 and 2520). The award of the Japan CAA, therefore, was not a provable debt and the referee in bankruptcy was correct in ruling that he was empowered to look behind the award and examine the merits of the claim and counterclaim.

Copal now maintains that Fotochrome withdrew from the arbitration and thus was not denied due process of law. The facts, however, clearly demonstrate that Fotochrome did not withdraw from the arbitration. From December 21, 1967 through January 27, 1970, the Japan CAA conducted 16 hearings, all of which were solely devoted to the reception of evidence offered by Copal (110a). Two of Fotochrome's witnesses were scheduled to testify at the 15th and 16th sessions. When Fotochrome was unable to present these witnesses -- the records fails to reveal the reason -- a 17th session was scheduled for March 31, 1970. Prior to the 17th session, however, Fotochrome filed a petition for an arrangement. Fotochrome's counsel did not refuse, as Copal now argues, to present Fotochrome's witnesses. He stated to the arbitrators that he "could" not present his witnesses at that session (110a).

Counsel's position was correct; the stay of the bankruptcy court prohibited Fotochrome from proceeding with the arbitration.

The arbitrators did not consider Fotochrome's inability to present its winesses on March 31, 1970 as a withdrawal from the proceedings. Their decision was not entered upon a default. To the contrary, they proceeded with the arbitration in Fotochrome's absence. They did not reject Fotochrome's defense and counterclaims on account of its failure to present its witnesses on March 31, 1970. Rather, their decision purports to rule on the defense and counterclaims upon the basis of the written statement submitted by Fotochrome at the outset of the proceeding and two exhibits submitted during the presentation of Copal's case (40a). Clearly, Fotochrome was denied due process of law.

POINT II

Copal's Reliance Upon Riehle v. Margolies is Misplaced

In Riehle v. Margolies, 279 U.S. 218 (1929), the Supreme Court held that a judgment obtained against a debtor by default in an action commenced by a creditor prior to the appointment of an equity receiver, established the existence and amount of the creditor's claim in a federal equity receivership, even though the receiver failed to defend the action. The court ruled that since the receiver was barred by Section 265 of the Judicial Code (28 U.S.C. §379) from enjoining the creditor's unit, the creditor was, therefore, entitled to have the judgment accepted as an adjudication of the existence and amount of the indebtedness. Justice Brandeis, speaking for the court, noted that this rule did not apply to bankruptcy proceedings where the power to stay is not limited by the Judicial Code. He expressly excluded from the opinion any consideration of the rule in bankruptcy.

> There are some cases arising under the Bankruptcy Act and some under state insolvency laws in which a judgment recovered in the state court was held not to be conclusive in the bankruptcy or insolvency proceedings. Thus, it has been held by some lower federal courts that

> a judgment recovered after institution of bankruptcy proceedings in an action commenced in a state court prior thereto, on a claim to which the limited power to stay action in a state court conferred by §11 of the Act of July 1, 1898, c. 541, 30 Stat. 549 applies, is not to be accepted in bankruptcy as conclusive proof of the claim. . . . These decisions are not inconsistent with the conclusion stated above. They have no application to receiverships in a federal court sitting in equity, which lacks the power to stay an action in the state court.

Accordingly, as noted in 1A Collier on Bankruptcy, 14th Edition §11, p. 1187, the lower federal court cases -- In re Service Appliance Co., Inc., 39 F.2d 632 (N.D.N.Y. 1930); Rhodes v. Elliston, 29 F.2d 737 (5th Cir. 1928), affirming In re Barrett & Co., 27 F.2d 159 (S.D. Ga. 1928); In re James A. Brady Foundry Co., 3 F.2d 437 (7th Cir. 1924) -- must be examined, and from them it appears that a judgment obtained in a suit pending at the commencement of bankruptcy proceedings does not bind a trustee unless he was made a party to the suit and directed by the bankruptcy court to defend it.

POINT III

Fotochrome was not Bound to Seek Relief from the Arbitral Award in the Courts of Japan

Copal argues that Fotochrome could have commenced an action in Japan to cancel the arbitrators' award, and its

failure to undertake such a course of action bars it from now raising questions of due process. In each of the cases relied upon by Copal in support of its position, the foreign arbitrators clearly had jurisdiction over the American party to the dispute (see cases cited at pp. 26 and 27 of Copal's brief). The Japan CAA, however, did not attain jurisdiction over Fotochrome as debtor in possession. Thus, the cases cited by Copal are inapposite.

Copal's position, moreover, disregards the fact that it filed a proof of claim in the bankruptcy court immediately after the arbitrators delivered their decision. It was Copal who provided the bankruptcy court with the jurisdictional prerequisite to an examination of the due process claim.

CONCLUSION

The decision and order of the lower court should be reversed.

Respectfully submitted,

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Services of ~~three (3) copies~~ 2 copies of
the within Reply Brief is
hereby admitted this 21ST day
of January, 1975

Whitman & Ransom
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